TOH PEE HENG & ANOR A

v.

MALAYSIAN ASSURANCE ALLIANCE BHD & ANOR

HIGH COURT MALAYA, KUALA LUMPUR B
LAU BEE LAN J
[CIVIL SUIT NO: S-22-879-2010]
5 OCTOBER 2013

INSURANCE: *Fire insurance - Consequential loss insurance - Liability - Whether plaintiff indemnified under insurance policy - Whether insurer liable - Whether plaintiff suffered consequential loss in business due to fire* C

INSURANCE: *Fire insurance - Consequential loss policy - Whether there was consequential loss incurred - Claim for losses suffered - Method of computation - Whether customary approach used in loss adjusting* D

EVIDENCE: *Witness - Conflicting evidence - Consequential loss - Claim for losses suffered - Method of computation - Whether claim allowed*

The plaintiffs insured their premises and stock in trade against fire E with the defendant insurance company *vide*, *inter alia*, Policy No. 010600249181-00 for Fire Consequential Loss, effective from 7 May 2006 to 6 May 2007. A fire broke out at the plaintiffs' factory premises and the plaintiff informed the defendants of the fire at the factory on 27 October 2006. The sole issue was in F respect of consequential losses. The defendants denied liability on the Fire Consequential Loss policy on the ground that there was no consequential loss incurred and thus the said policy was not at risk. The plaintiffs contended that they had incurred consequential losses and the defendants were liable based on the G Fire Consequential Loss policy. PW2, the sole proprietor of Hang Tien Enterprise (first plaintiff) and Gong Guan Trading (second plaintiff) testified that the fire completely destroyed Lot 1-14 where all his stocks were kept. As a result of the fire, it was alleged that all the recycled materials were ruined. Due to this, he lost his H customers as he was unable to supply to their needs. PW1, an audit partner of the firm gave a detailed explanation of the computation of the consequential losses by using the quarterly time periods as basis of computation since the maximum period of indemnity was six months or two quarters. PW1 also computed I

the compound growth per quarter by taking the fourth quarter of the 2005 earnings and third quarter of the 2006 earnings just before the fire. PW1 found a compounded growth rate of 50.53% per quarter during the period of 2006 that would result in RM2,292,071 turnover in the six months following the fire. PW1 further agreed that a further amount of sales of RM299,000 was to be deducted from the above figure to give a revised lost turnover of RM2,063,071. PW1 used a gross profit rate of 33.38% to arrive at a figure of RM664,000 as the consequential losses post fire as per Bundle B1/1-7. On the contrary, DW1, an Assistant General Manager at an international loss adjusters company, testified that he prepared a Mclaren's Young International First and Final Report Commercial – Business Interruption ('Mclaren's Report') for the defendant and gave evidence that his investigations and analysis did not disclose any consequential loss. However, DW1 did not refer the court to the method of computation but merely mentioned that he was using a customary approach in loss adjusting. DW1 did not agree with the quarterly growth rates employed by PW1 as the compound growth rate of 50.53% was too high. DW1 stated that the return on shareholders' fund had declined from 77.26% in 2004 to 36.73% in 2005 and 33.49% in 2006. When queried as to the formula used by DW1 in arriving at those figures, DW1 stated that the formula worked on the profit before tax divided by shareholders' fund. Following this formula, DW1 agreed that the profit before taxation of RM101,946.47 in 2004 has gone up to RM105,024.72 in 2006. The court was faced with the conflicting evidence of the experts from both parties. The issues that arose for determination, *inter alia,* were (i) the approach to be adopted when dealing with the expert evidence of PW1 and DW1; (ii) whether the plaintiffs suffered any consequential loss due to the fire; and (iii) whether the defendants were liable under Policy No. 010600249181-00 to indemnify the plaintiffs for the consequential losses suffered due to the fire.

Held (allowing plaintiffs' claim with costs):

(1) It was incumbent for the court to determine the credibility of the experts and make a finding whether the findings of the experts were substantiated. DW1 did not refer the court to the method of computation as per the policy but merely submitted that he used a customary approach in loss

adjusting. DW1's approach was vague compared to the review conducted by PW1 in accordance with international standard on auditing to review whether the loss of profit computation was free of material misstatement. On a balance of probabilities, the court agreed with the plaintiff's submission that the plaintiff's use of 50.53% was reasonable and was supported by the detailed workings at Bundle B1/1-7. *Chua Seng Sam Realty Sdn Bhd v. Say Chong Sdn Bhd & Ors And Other Appeals*; refd. (paras 19 & 20)

(2) On a balance of probabilities, DW1 agreed that (i) the return on shareholders fund was obtained by dividing the gross profit before tax with the shareholders' fund; and (ii) the profit before taxation of RM101,946.47 in 2004 had gone up to RM105,024.72 in 2006. Therefore, the court was inclined to agree with the plaintiffs' submission that the return on shareholders' fund was high by any standard and the second plaintiff was a profitable company. (para 20)

(3) Taking the plaintiffs' two lines of business which were plastic parts manufacturing and trading of raw material, the plaintiff had shown based on the total sales for six months before the fire was RM777,440 and the total sales after the fire was RM299.353.25. There was a drop in sales of RM478,087. In this regard, the court was inclined to agree with the plaintiffs' submission that there was a consequential loss because of the fire. (para 20)

(4) The consequential loss policy payment conditions occurred under two scenarios, *ie*, loss of gross profit due to reduction in sales or turnover; or when there was an increase cost of working, increase in cost of working in order to prevent reduction in sales or turnover. In the case of the second plaintiff, the consequential loss arose in respect of loss of profit due to reduction in sales or turnover. Thus, the plaintiffs had proved that they suffered losses covered by the Policy No. 010600249181-00 for fire consequential loss. (paras 25 & 26)

Case(s) referred to:

Chua Seng Sam Realty Sdn Bhd v. Say Chong Sdn Bhd & Ors And Other Appeals [2012] 7 CLJ 337 CA ***(refd)***

Legislation referred to:
Insurance Act 1996, s. 22

For the plaintiffs - G Gunaseelan (R Selvarajoo with him); M/s G Gunaseelan & Assocs
For the defendants - Andrew Khoo; M/s Khoo & Sidhu

Reported by Sandra Gabriel

JUDGMENT

Lau Bee Lan J:

Background

[1] The plaintiffs insured their premises and stock in trade against fire with the defendant insurance companies *vide* these policies:

(a) Policy No. 010600249181-00 was for "Fire Consequential Loss" (Bundle B pp. 6-30 (Bundle B/6-30)); and

(b) Policy No. 010600247068-00 was for "Damage to Stock in Trade Office Equipment and Machinery" (Bundle B/1-5 - Policy Schedule).

[2] Both policies were effective for the period 7 May 2006 to 6 May 2007.

[3] It is not disputed that from the copies of the policy schedule (Bundle B/10-20), the policy is (i) a "TARIFF" policy ie, a type of policy issued is a standard wording of policy issued by all insurers in Malaysia pursuant to s. 22 of the Insurance Act 1996; and (ii) the maximum indemnity period is for six months and the basis for payment is on gross profit.

[4] There was a fire at the plaintiffs' factory premises at No. 1-14, Jalan Perindustrian 2, Kawasan Perindustrian Bukit Bakri, 84200 Bukit Bakri, Johor Darul Takzim.

[5] The plaintiff informed the defendants of the fire at the factory on 27 October 2006.

[6] The defendants have settled the insurance payments in respect of the stock in trade, office equipment and machinery on 31 July 2007 for RM740,000. However the sole issue is in respect of consequential losses.

[7] The defendants have denied liability on the "Fire Consequential Loss" policy on the ground there was no consequential loss incurred and therefore the said "Fire Consequential Loss" policy was not at risk.

[8] However, the plaintiffs contend there were consequential losses and the defendants are liable on the "Fire Consequential Loss" policy.

Issues

[9] The agreed issues to be tried are:

(a) Whether the plaintiffs have suffered any consequential loss due to the fire?

(b) Whether the defendants are liable under the Policy No. 010600249181-00 to indemnify the plaintiffs for the consequential losses (if any) suffered due to the fire?

Findings

Whether The Plaintiffs Have Suffered Any Consequential Loss Due To The Fire?

[10] Apart from the undisputed background facts, the evidence is Mr Toh Pee Heng (PW2), the sole proprietor of Hang Tien Enterprise (first plaintiff) and Gong Guan Trading (second plaintiff/ Gong Guan) stated his factory is situated at Lot No. 1-13, 1-14 and 1-29 but the fire completely destroyed Lot 1-14 where all his stocks were kept.

[11] He further testified that his major client is Joubert through an intermediary known as Technecon but he has other clients such as Pariplas Industries Sdn Bhd, Inpoh Industries Sdn Bhd, CMI and Jin Kong. He has two lines of business producing plastic products and trading in recycled materials. He stated that because of the fire all the recycled products/materials were ruined and the recycling business was gone. He had lost his customers because he was not able to supply their needs.

[12] He stated the plaintiffs are covered under the consequential losses for the sum of RM1,500,000. He was claiming about RM765,093, the sum worked out from the profit and loss accounts of Gong Guan from 2004 to 2006 which was used as base by the Chartered Accountants Yong & Leonard to explain the amount of consequential loss claimed (Bundle B1/1-23 and 45-65).

[13] Mr Leong Pooi Wah (PW1), the audit partner of the firm of Chartered Accountants, Yong & Leonard testified that Gong Guan was involved in principally two lines of businesses (i) plastic manufacturing; and (ii) trading in raw materials. He stated that his firm's role is to review the loss of gross profit computation of Gong Guan which is not an audit and therefore they are expressing any audit opinion and based on their review "nothing has come to our attention that causes us to believe that the loss of gross profit computation not giving a true and fair view in accordance with Malaysian Accounting Standards applicable to entities other than private entities" (Bundle B1/1-7).

[14] He gave a detailed explanation of the computation of the consequential losses. As summarised by the plaintiffs, PW1 stated:

(a) he used quarterly time periods as basis of computation as the maximum period of indemnity was six months or two quarters;

(b) he computed the compound growth per quarter by taking the fourth quarter 2005 earnings and third quarter 2006 earnings (just before the fire). He found a compounded growth rate of 50.53% per quarter during that period of 2006 and would result in RM2,292,071 turnover in the six months following the fire;

(c) he agreed that a further amount of actual sales of RM299,000 is to be deducted from the above figure to give a revised lost turnover of RM2,063,071.

(d) he used a gross profit rate of 33.38% to arrive at a figure of RM664,000 as the consequential losses post fire.

(Notes of Evidence (NOE) Vol. 1/73-76; Bundle B1/1-7)

[15] Mr Tan Chiap Yeong (DW1), currently the Assistant General Manager at M/s McLaren Saksama (Malaysia) Sdn Bhd in Johor Bahru, an international loss adjusters company and who

was the manager in 2006-2007 testified (i) he prepared the McLarens Young International First and Final Report Commercial - Business Interruption dated 16 August 2008 (Bundle B1/pp. 24-87) (McLarens Report) for the defendant and (ii) his investigations and analysis contained in pp. 27-36 of the McLarens Report does not disclose any consequential loss.

[16] In the present case this court is faced with the conflicting evidence of the plaintiffs' expert, PW1 and the defendant's expert, DW1 and the question which arises is what is the approach to be adopted in dealing with both the expert evidence. In *Chua Seng Sam Realty Sdn Bhd v. Say Chong Sdn Bhd & Ors And Other Appeals* [2012] 7 CLJ 337, the first plaintiff company, the registered owner of the land erected a retaining wall below the bungalow occupied by the second and third plaintiffs, the shareholders and directors of the first plaintiff company. The first defendant leased her land which was adjacent to the first plaintiff's land to the second defendant who decided to build a bungalow. The excavation work began on the first defendant's land and the first plaintiff's retaining wall collapsed resulting in a landslide. The plaintiffs commenced legal action against the defendants alleging that the excavation work was carried out in a negligent manner. The first and second defendants counterclaimed against the first plaintiff alleging that the first plaintiff was negligent in constructing and maintaining the safety of the retaining wall resulting it in collapsing and causing damage to the first and second defendants' land. Both the plaintiffs' expert witness and the defendants' expert witness gave differing evidence as to the cause of the collapse of the retaining wall.

[17] The Court of Appeal at para. 48 at p. 349 opined:

> In the present case, the court was faced with two conflicting expert evidence on the cause of the collapse of the first plaintiff's wall. In treating conflicting expert evidence, the court, besides examining the credibility of the experts, should also examine the scientific grounds and facts relied by the experts relied and whether, when taken in totality, the inferences drawn from their findings are sound or otherwise (see *Singapore Finance Ltd v. Lim Kah Ngam (S'pore) Pte Ltd & Eugene HL Chan Associates (Third Party)* [1984] 1 LNS 3).

[18] On that score the Court of Appeal held the learned High Court Judge had erred in giving undue weight to the evidence of the plaintiffs' expert but failed to give due consideration to the

defendants' expert witness who had prepared three reports on the cause of collapse of the first plaintiff's retaining wall; two reports were based on his investigation on site and the third report was based on drawings supplied by the first plaintiff as opposed to the first plaintiff's expert report was prepared by his engineer who was never present during any site visits.

[19] From the case of *Chua Seng Sam Realty Sdn Bhd* (*supra*) it is incumbent for the court to determine the credibility of the experts and make a finding whether the findings of the experts are substantiated by scientific grounds and facts and sound inferences are drawn thereon.

[20] Through the cross-examination of DW1 I have found his evidence to be flawed or the evidence of PW1 to be more credible as shown below:

(a) DW1 did not refer the court to the "method of computation" as per the policy and is nowhere found in the Common Bundles of Documents but merely said he was using a "customary approach in loss adjusting". In the "customary approach in loss adjusting" DW1 said (i) he looked into the plaintiffs' sales generated from the production of plastic parts and the sales of trading of raw material; (ii) the actual sales achieved from the production of the plastic parts after the fire and compare that against before the fire on a like to like basis and then the result obtained is again checked against the policy conditions (NOE Vol. 2/131-132).

(aa) In my view DW1's approach is rather vague when compared to the review conducted by PW1 made in accordance with International Standard on auditing applicable to review engagements which standard "requires that we plan and perform the review to obtain moderate assurance as to whether the loss of profit computation is free of material misstatement" and supported by the computation at Bundle B1/1-7.

(b) DW1 did not agree with the quarterly growth rates employed by PW1 as he felt that the compound growth rate of 50.53% was too high. However he agreed that the annual growth rate based on the years 2005 and 2006

was 82%. During re-examination, when asked to explain why he disagreed to the figure of 50.53% used by PW1, DW1 merely said "I would need a scientific calculator to work that out actually" and thereafter when asked "If it's 50.53% per quarter, on a quarterly basis per year it will be more than 50% per year", DW1 agreed (NOE Vol. 2/136-139).

(bb) On a balance of probabilities, based on the evidence, I agreed with plaintiff's submission that the plaintiff's use of 50.53% was reasonable and was supported by the detailed working at Bundle B1/7 (NOE Vol. 2/68-69).

(c) Premised on what DW1 said that he looked into the plaintiffs' sales generated from the production of plastic parts and the sales of trading of raw material, I agreed with the plaintiffs' submission that DW1's position that there was no growth in 2006 post fire is flawed because he neglected to take into account the trading of raw materials, plaintiffs' second line of business when he has agreed that (i) the raw materials were burnt in the fire; and (ii) he completely ignored the sales of materials which amounted to RM823,000 before the fire to compute the losses subsequent to the fire (NOE Vol. 2/135 - 136). In re-examination when DW1 was asked why was there no column for materials noted after the fire, he replied "The plaintiff informed us that they do not have sufficient cash flow to trade … To deal with the trading business".

(cc) Learned counsel for the plaintiffs requested the court to record his objection to the answer of DW1. I find there is merit in plaintiffs' objection because there is no record supportive of that statement in the McLarens report and the answer of DW1 "The insured advised us that no materials were sold during this period due to tight cash flow" is not the same as him saying "The plaintiff informed us that they do not have sufficient cash flow to trade … To deal with the trading business". (NOE Vol. 2/155-156).

(ccc) Taking the two lines of business of the plaintiffs, plastic parts manufacturing and the trading of raw material, the plaintiff had shown based on the total sales for six months before the fire was RM777,440 (May to October 2006)

A and the total sales after the fire was RM299,353.25 (November 2006 to April 2007), a drop in sales of RM478,087. DW1 agreed that the plastic and the raw materials were burnt in the fire coupled with the fact that the plaintiffs did not have enough capital to resume the
B business and that the indemnity payment for the stock in trade was paid much later, the plaintiffs were unable to resume the business of trading in raw materials immediately (NOE Vol. 2/124-125 & 136). In this regard I am inclined to agree with the plaintiffs' submission there was a
C consequential loss because of the fire.

(d) DW1 stated the return on shareholders fund had declined from 77.26% in 2004 to 36.73% in 2005 and 33.49% in 2006 (Bundle B1/29). DW1 disagreed with the plaintiffs'
D proposition that the decrease in the "return of shareholders' fund" was because the shareholders' fund "has been increasing from 2004 to 2006, that means to say that the profits have been used to top the shareholders' fund". DW1 stated he disagreed because
E despite the increase in annual turnover from RM845,271.50 (2004) to RM1,279,795 (2006) but the gross profit reduced from RM372,775 (2004) to RM273,347.95 (2006). When queried as to the formula he used in arriving at the figures of 77.26%, 36.73% and
F 33.49%, he stated that "The formula works on the profit before tax divided by shareholders' fund … That means it measures … profit you earn against the amount of money injected into the company". Following this formula, he agreed that the profit before taxation of RM101,946.47 in
G 2004 has gone up to RM105,024.72 in 2006; however he disagreed when cross-examined on whether the shareholders' funds significantly increased from 2004 to 2006 but later said "On paper, yes. But you got to look at the ratio of how effective it is". (NOE Vol. 2/102-105).

H When re-examined on this point DW1 pointed the court to Bundle B1/29 "return of shareholders' fund" stating "So this is a ratio which measures how effective the shareholders' fund performed in the business … In 2004
I the ratio was 77.26% … In 2006 it went down to become 33 cents from RM1 of shareholders' fund … meaning RM1 of shareholders fund could only earn 33 cent (sic) now." (NOE Vol. 2/143-144).

(dd) On a balance of probabilities, since DW1 himself (i) agreed that "return on shareholders fund" is obtained by dividing the gross profit before tax with the shareholders' fund, (ii) he also agreed profit before taxation of RM101,946.47 in 2004 has gone up to RM105,024.72 in 2006 and (iii) even if the "return on shareholders' fund" was reduced from 77.26% in 2004 to 33.49% in 2006, I am inclined to agree with the plaintiffs' submission that the "return on shareholders' fund" is "high by any standard" if the court compares the fixed deposit rates at the local banks is only 2% to 4.5% per year and Gong Guan was a profitable company. This was in fact acknowledged by DW1 in his report as "Overall, with continuous orders from Joubert, we believe that Gong Guan Trading is an ongoing and profitable business entity prior to the fire. There was no evidence that the business operations were declining or going to be shut down". (Bundle B1/30).

(e) DW1 raised the issue of increase in total borrowing by Gong Guan from RM177,845.60 (2004) to RM458,435.90 (2006) but he did not as submitted by the plaintiffs show that it was detrimental to profitability (NOE Vol. 2/99).

(f) PW1 agreed in re-examination that the McLarens Report at B1/35 stated (i) "The closing stocks as at September 2006 was MYR1.7 million.", (ii) the stockholdings in 2006 was 489 days (B1/29), (iii) the stocks should include the raw material, finished product plus work in progress, (iv) stocks (raw materials kept in the store) cannot be used to produce any goods and the stocks which has been burnt is a loss and there is loss of opportunity to make sales and this is a supporting factor for the consequential loss (NOE Vol. 2/59-63). This closing stock as at September 2006 of RM1.7 million was also taken into account by DW1 who in cross-examination agreed (i) that these stocks included finished products, semi-finished products and raw materials, and (ii) whilst the finished products and raw materials were valued on selling price, the raw materials were based on cost. On a balance of probabilities the value of the stocks at September 2006 if sold in the course of business would have made at least RM1.7 million.

A

Other Matters

[21] Learned counsel for the defendant submitted that the plaintiffs ought to call PW2's sister as a witness since PW2 had admitted he did not prepare the accounts but it was prepared by his sister, Toh Siew Cheng, who certified at Bundle B1/10 and 13 and PW1 stated that Bundle B1/5-7 were prepared by PW2's consultants.

B

[22] In my view it is not necessary to call PW2's sister as a witness because (i) the accounts for Gong Guan for the period 2004-2006 were not disputed but was incorporated without qualification by DW1 into the McLarens report; and (ii) unlike DW1 who said he was using a "customary approach in loss adjusting", PW1 stated the review was conducted in accordance with international standard on auditing.

C

D

[23] Learned counsel for the defendant submitted PW1:

> Initially alleged/claimed that evidence of invoices before and after the fire and supporting documents for the profit and loss accounts was not appropriate for the purposes of calculating the forecast and projections of gross profit (NOE Vol. 1/23-24).
>
> However, when asked to confirm whether in order to confirm if the forecast of a profit is right, bearing in mind that the business in this case was ongoing/continuous after the occurrence of the fire, that turnover and sales and profit and loss after the fire was relevant, SP1 admitted that these should be taken into account (NOE Vol. 1/25-26).

E

F

[24] This concern of the defendant has been taken into consideration. As alluded to earlier, DW1 has agreed to reduce the projected turnover by the actual turnover during the relevant period to arrive at the true loss of sales/turnover computed as follows:

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Projected Loss of sales/turnover	RM2,292,071.00
Less Actual sales/turnover	RM 299,000.00
Net loss of sales/turnover	RM2,063,071,00
Loss of Gross Profit (33.38/100 X 2,063,071)	664,000

H

I

(NOE Vol.1/78)

Whether The Defendants Are Liable Under The Policy No. 010600249181-00 To Indemnify The Plaintiffs For The Consequential Losses (If Any) Suffered Due To The Fire?

[25] SD1 stated the consequential loss policy payment conditions occurred under two scenarios:

(a) loss of gross profit due to reduction in sales or turnover; or

(b) increase cost of working, increase in cost of working in order to prevent reduction in sales or turnover.

[26] In the case of Gong Guan, DW1 stated the claim for consequential loss arises in respect of loss of profit due to reduction in sales or turnover. Thus for all the reasons discussed in paras. 19 to 24 above, I find the plaintiffs have proven that they suffered a loss covered by the Policy No. 010600249181-00 for "Fire Consequential Loss."

Conclusion

[27] In the circumstances the court allowed the plaintiffs' claim as follows:

(a) Defendant is to pay to the plaintiff the sum of RM664,000;

(b) interest at the rate of 4% per annum on the said sum of RM664,000 from the date of writ of summons till the date of judgment;

(c) interest at the rate of 5% on the said sum of RM664,000 from the date of judgment till the date of realisation; and

(d) Defendant is to pay costs to the plaintiff fixed at RM50,000.